No. 9454

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

In the Matter of

FRED WILLIAMS,

Bankrupt.

WILLIAM I. HEFFRON, as Trustee of the Estate of FRED WILLIAMS, Bankrupt,

Appellant,

vs.

BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION,

Appellee.

BRIEF OF APPELLANT.

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Opinions Below.

The only previous opinions in this case were The Decision of the Referee in Bankruptcy [Tr. of R. pp. 49-84], Memorandum of Order of the District Judge [Tr. of R. pp. 154-156].

Statement of Pleadings and Facts Disclosing Basis of Jurisdiction.

Fred Williams was adjudicated bankrupt by the District Court of the United States, Southern District of California, Central Division, on September 25, 1937, and further proceedings in that matter referred to Ernest R. Utley as Referee in Bankruptcy [Tr. of R. pp. 3, 4]. The appellant qualified as Trustee in Bankruptcy October 15, 1937. [Tr. of R. p. 5.]

The appellee, Bank of America National Trust and Savings Association, filed its Proof of Secured Debt with the Referee February 7, 1938 [Tr. of R. pp. 6-14], by which appellant claimed as security to indebtedness of $14,790.76 certain steel with an asserted value of approximately that amount.

February 9, 1938, appellant filed objections to the claim [Tr. of R. pp. 14-19], in response to which objections the appellee filed its answer [Tr. of R. pp. 20-39]. After a partial hearing, on March 18, 1938, appellant filed amendments to objections [Tr. of R. pp. 40-42], in response to which, on March 31st, appellee filed an answer [Tr. of R. pp. 43-49]. After hearing in connection with the foregoing, on July 11, 1938, the Referee made Findings of Fact, Conclusions of Law, and Order [Tr. of R. pp. 85-103], whereby, among other things, the claim of appellee was disallowed in its entirety as a secured claim, and allowed in its entirety as an unsecured general claim. Subsequently, and within the time prescribed by law, to-wit: on July 25, 1938, appellee filed Petition for Review of Referee's Order [Tr. of R. pp. 104-116]. Subsequently, the District Court reversed the Order of the Referee and allowed the appellee's claim as a secured claim by Minute Order [Tr. of R. pp. 156-157] filed November 3, 1939,

and by formal order filed December 8, 1939 [Tr. of R. pp. 157-162]. No written notice of either of said orders was served or filed, and on December 13, 1939, Notice of Appeal [Tr. of R. pp. 163-164], Assignment of Errors, and Statement of Points on which appellant will rely in this appeal [Tr. of R. pp. 164-166], and Petition for Appeal to the Circuit Court of Appeals, Ninth Circuit [Tr. of R. pp. 166-169], were filed, the latter being allowed December 13th [Tr. of R. p. 167].

Under section 2 of the Bankruptcy Act the District Court had jurisdiction to determine the validity of the security claimed by appellee. Sections 24 and 25 of the Bankruptcy Act sustained jurisdiction of the Circuit Court of Appeals in respect to this appeal, and the appeal is taken pursuant to said sections and pursuant to rules 73, 75 and 76 of the Federal Rules of Civil Procedure.

Statement of Case and Questions Presented.

In making statement of facts of the case and of the questions presented, the appellant takes as a foundation the order of the District Court entitled "Order Reversing Order of the Referee Re Claim of Bank of America National Trust & Savings Association" [Tr. of R. pp. 157-162], wherein it is stated, among other things, "The court hereby adopts the Findings of Fact made by the said Referee and contained in the Referee's Findings of Fact, Conclusions of Law, and Order, with the following exceptions: . . .", together with Memorandum of Order of the District Court [Tr. of R. pp. 154-156].

It appears, from the Findings of the Referee, confirmed by the District Court, that from the year 1935 the bankrupt, under the name of General Steel Co., was a wholesale

and retail merchant in the City of Los Angeles, where he had two places of business, one at 633 S. Anderson street, and the other at 512 S. Anderson street, and was engaged in the sale of unfabricated steel of various kinds and dimensions with an inventory, the value of which, based on cost to him in Los Angeles, was around $29,000.00. At the former address he maintained his office and kept a portion of his inventory. At the latter address he kept the remainder of inventory because of lack of space at the former address. Deliveries were made from the office address. During the period from April 1st, 1937 to September 14th, 1937 the bankrupt made 701 sales in amounts ranging from 41¢ to $1779.51, the average amount of each sale being approximately $99.36. Other than salesmen on the outside soliciting orders and contacting prospective customers, the bankrupt had in his employ two stenographers in the office and one regular employee by the name of Rinne who was paid $30.00 per week. From April, 1936 to July 20, 1937, Rinne's duties consisted of being janitor, answering telephone calls, driving a truck and keeping stocks straight, locking up the premises at night, and general work of this nature.

The premises at 663 S. Anderson street consisted of a one-story building. A small portion of the front of the building was used by the bankrupt as his office, and the balance of the building was used for the storage of steel, it being separated from the office portion by walls or partitions. Access from the office to the balance of the building could be had through a double door of ordinary size. There were two large truck entrances to the storeroom portion, one from the front and one from the rear of the building.

Prior to his dealings, hereinafter referred to, with Lawrence Warehouse Co. and the appellee, Bank of America National Trust & Savings Association, the bankrupt became indebted to numerous creditors who had general unsecured claims which were unpaid at the time of filing of the bankruptcy proceeding, which claims became provable and were filed and allowed in the bankruptcy proceedings. These claims arose through the purchase of steel.

During the month of July, 1937, the bankrupt decided that he would like to borrow some money upon his supply of steel and pursuant thereto, and on July 20, 1937, he entered into a leasing agreement and a field warehouse storage agreement with the Lawrence Warehouse Company, which will hereafter sometimes be referred to as the Warehouse Company. Under this lease and agreement, the bankrupt purported to lease to the Warehouse Company all of the building at 663 South Anderson street, with the exception of the office, for the yearly rental of $1.00, and, subsequently, under date of August 20, 1937, he purported to lease an adjoining lot under similar terms to the Warehouse Company. The lot in question was enclosed on three sides by a strong woven wire fence and on the remaining side by the wall of the building. No goods were stored in this lot.

Under the agreement, the Warehouse Company was to act as custodian of all goods which the bankrupt then had on the premises and of any other goods which should be placed on the premises. The agreement further provided that the Warehouse Company could store goods of other persons upon the premises if it so desired, but it was not the intention of the parties or the practice of the Ware-

house Company to store goods of other persons on the premises, nor were any such goods stored.

Pursuant to the terms of the agreement, the Warehouse Company was to furnish a "bonded agent" or "bonded watchman" in charge of the warehouse and of the merchandise stored therein. The cost of this agent or watchman was to be included in the charges for warehouse services furnished by the Warehouse Company to the bankrupt; and was to be paid in advance on the first day of each month during the life of the agreement. The bankrupt, in addition, agreed to pay the Warehouse Company for all other warehouse labor performed by employees of the Warehouse Company, and for all taxes imposed upon the operation of the warehouse, and all other expenses incidental to the conduct of the warehouse, plus fifty cents per ton per month, or fraction thereof, for the storage of the steel from the date of the issuance of each warehouse receipt.

Rinne, who had previously been working for the bankrupt, as pointed out above, was hired by the Warehouse Company as such agent or watchman. He was paid by the Warehouse Company for his services to it the same amount of compensation per month he had previously received when he was working for the bankrupt; and the bankrupt, in paying the charges of the Warehouse Company, included in such amount the compensation paid by the Warehouse Company to Rinne. Excepting that he no longer drove a truck, Rinne continued to do about the premises the same character of work he had been doing up to July 20, 1937, and, in addition, performed certain other duties for the Warehouse Company hereafter adverted to. No other compensation was paid to him for his services than the amount already indicated.

Padlocks bearing the name of the Warehouse Company were placed on the entrances to the warehouse portion of the premises, the keys being retained by Rinne, who, however, permitted the bankrupt to have access to the premises. Several metal signs, in size about 9″ x 20″, each bearing the name of the Warehouse Company in large letters and a statement to the effect that "all commodities in or upon these premises are in the custody of the Lawrence Warehouse Company, Lessee" and the words "No Trespassing", were placed at the various entrances to the portion leased by the Warehouse Company, and after August 20, 1937, on the fence enclosing the lot leased on August 20, 1937. There was no Warehouse Company sign over the outside entrance to the office of the building, but inside the office and immediately over the double doors leading to the store room portion of the building was such a sign. Several such signs were also posted in several places where they could be seen inside the warehouse portion, one of them being on a partition of a small toilet or washroom a few feet inside the front truck entrance and facing directly toward the entrance. Another was placed upon the trussing about ten feet above the floor.

All of the steel in the store building at 663 South Anderson street at the time the original lease was entered into with the Warehouse Company, remained there, excepting such withdrawals as were made in the ordinary course of trade.

On or about July 28, 1937, the Warehouse Company issued three non-negotiable warehouse receipts, being respectively numbered and covering steel of the cost to the bankrupt, follows: as No. 4201 covering goods of the cost of $776.20; No. 4202, covering goods of the cost of

$1982.06, and No. 4203 covering goods of the cost of $2180.03, the total cost to the bankrupt of such steel being $4038.29. By the terms of said receipts the Warehouse Company acknowledged receipt from the bankrupt of the goods therein described and agreed, among other things, to hold them subject to the written order of the California Bank. The receipts were delivered by the Warehouse Company to the bankrupt and thereafter delivered by the bankrupt to the California Bank as asserted collateral for a present loan made by the California Bank to the bankrupt in the sum of $3000.00.

About August 1, 1937, the bankrupt entered into negotiations with the claimant herein to borrow certain moneys from the claimant. In connection with such negotiations, and on August 3, 1937, the bankrupt caused to be issued by the Warehouse Company additional non-negotiable warehouse receipts similar in form to the ones above mentioned, excepting that the goods were to be held for the written order of the claimant. The numbers of such receipts were as follows: No. 12902 covering goods of the cost to the bankrupt of $1832.58; No. 12903 covering goods of the cost to the bankrupt of $1039.84; No. 12904 covering goods of the cost of $1113.56; No. 12905 covering goods of the cost of $1565.77; No. 12906 covering goods of the cost of $1685.78; No. 12907 covering goods of the cost of $1340.85; and No. 12908 covering goods of the cost of $2192.96. The total cost to the bankrupt of all the goods covered by such receipts was the sum of $10771.34. The receipts were delivered by the Warehouse Company to the bankrupt, and thereafter, on August 5, 1937, delivered by the bankrupt to the claimant as asserted collateral for a present loan made by the claimant to the bankrupt in the sum of $8170.59.

Thereafter, additional non-negotiable receipts similar in form were issued by the Warehouse Company, as follows: On August 16, 1937, No. 12910 covering goods of the cost to the bankrupt of $747.11, and No. 12911 covering goods of the cost of $1897.76; No. 12912 covering goods of the cost of $1199.01; No. 12913 covering goods of the cost of $916.25; No. 12915 covering goods of the cost of $1081.54; No. 12916 covering goods of the cost of $744.62; and No. 12917 covering goods of the cost of $756.00. The total cost of the goods to the bankrupt was $7342.29. The receipts were delivered by the Warehouse Company to the bankrupt at or about the respective dates of such receipts, and thereafter, on August 17, 1937, delivered by the bankrupt to the claimant as asserted collateral for a present loan of $5506.72.

Thereafter, additional non-negotiable receipts similar in form were issued by the Warehouse Company, as follows: On August 23, No. 12919 covering goods of the cost to the bankrupt of $808.49 and No. 12920 covering goods of the cost of $1518.77; on August 24, No. 12921 covering goods of the cost of $2369.88, and No. 12922 covering goods of the cost of $816.82; on September 1, 1937; No. 12923 covering goods of the cost of $99.29; No. 13701 covering goods of the cost of $677.08; No. 13702 covering goods of the cost of $406.97; No. 13703 covering goods of the cost of $632.66; and on September 2, No. 13705 covering goods of the cost of $1946.67, and No. 13706 covering goods of the cost of $1529.39. The total cost of the goods covered by such receipts was the

sum of $10806.12. Such receipts were delivered by the Warehouse Company to the bankrupt at or about the respective dates of such receipts, and thereafter, on September 2, 1937, delivered by the bankrupt to the claimant as asserted collateral for a present loan of $3969.00

The goods covered by the receipts used in the California Bank loan were included in the receipts used in the loan of August 5, 1937, and the loan by the California Bank was paid off by the bankrupt from the proceeds of the loan of August 5th.

No notice of intention as provided in the Bulk Sales Law of the State of California (Section 3440 of the Civil Code) was recorded in the office of the County Recorder of Los Angeles County in connection with any of the transactions hereinabove enumerated, or at all.

As warehouse receipts were issued by the Warehouse Company to the bankrupt, cards designated as "Stack Cards" showing the name of the person for whose account the receipts had been issued and the name of the pledges and the amount of the steel covered by the receipts, were placed on the various piles of steel included in the warehouse receipts. The stack card described the steel by the number of pieces and their dimensions and referred to the warehouse receipts by number. All steel of the same dimensions was kept in separate piles or bins or shelves. A small band of wire in some instances was wrapped around some of the free goods but there were no marks of any kind on these bands or wires excepting that some of them were painted white. In many instances the free steel was commingled with the steel covered by the receipts in that the free steel was not physically separated from the pledged steel. One lot of steel had been pledged

by means of warehouse receipts to one Prezant about August 1, 1937, but no such cards were maintained on or around said steel.

The Warehouse Company took or kept no inventory or account of any of the goods within the premises at 663 South Anderson street excepting such goods as were covered in the warehouse receipts issued as hereinabove set forth. At all times, the bankrupt was permitted to and did engage freely in the sale of "free goods" located upon the premises and there was no requirement of the bankrupt to obtain permission of any kind from the Warehouse Company before making shipments from the premises of any steel not covered in the receipts. Such shipments were handled by Rinne or the bankrupt or both. No pledged steel was sold without first procuring a release. The bankrupt did not procure releases of pledged steel to fill particular orders, but when the supply of free steel of a particular dimension had been exhausted, the bankrupt applied for a release of a quantity of steel of that dimension. A form of request for release was prepared by Rinne from lists furnished by the bankrupt. These were taken by the bankrupt to the bank and its consent to release procured upon the form, a payment being made to the bank proportionate to the amount of steel being released. The bankrupt then took the release to the Los Angeles office of the Lawrence Warehouse Company, where an officer of the warehouse company signed an authorization to Rinne permitting him to release the goods. This release was then delivered to Rinne and the goods were accordingly released to the bankrupt.

A portion of the goods covered by the warehouse receipts were goods which were on hand and in the premises at 663 South Anderson street when the original lease was entered into. Other goods were thereafter moved from 512 South Anderson street to 663 South Anderson street and then warehouse receipts issued thereon. A portion of the goods covered by such receipts were goods which had been delivered to the bankrupt from Los Angeles Harbor about September 1, 1937, same having been purchased from Pacquet Company. These goods were delivered by flat car to 663 South Anderson street and receipts issued immediately. Such goods have not been paid for.

Under the bankrupt's agreement with the Warehouse Company, the only compensation payable to the Warehouse Company (other than a refund of actual costs incurred, such as Rinne's salary, bond premium, auditing expenses, etc.) was the sum of 50¢ per ton per month for only those goods stored which were covered by warehouse receipts, with a provision that there should be a minimum charge of $200.00 for the first ninety days or of $500.00 for the first year from the date of issuance of the first warehouse receipts.

The leases and warehousing agreement between the bankrupt and the Warehouse Company were not entered into for the purpose of maintaining storage or physical protection for the goods involved, but for the sole and only purpose of obtaining warehouse receipts in order that same could be used as collateral for loans to be obtained by the bankrupt. The claimant, before making any

of its loans to the bankrupt, had knowledge of such purpose.

At all times involved herein, the bankrupt was a retail and wholesale merchant engaged in the sale and purchase of steel. The claimant, before making any of its loans to the bankrupt, had knowledge of such fact.

At all times involved herein, the bankrupt had existing creditors. The claimant, before making any of its loans to the bankrupt, had knowledge of such fact.

The amount of goods involved in each loan by the claimant was a substantial portion of the stock in trade of the bankrupt. The claimant, before making any of its loans to the bankrupt, had knowledge of such fact.

During the times herein involved there was no custom that a retail or wholesale merchant (steel merchant) could pledge his goods without giving a seven-day notice to creditors; nor was there any custom of "field-warehousing" by steel merchants or jobbers in order to finance their business.

On or about November 22, 1937, the trustee made demand upon the claimant for the return to the trustee of the steel involved in the foregoing warehouse receipts, or in lieu thereof, for payment of the reasonable value thereof. The claimant failed and refused to deliver to the trustee said steel or any portion thereof; the claimant failed and refused to return to the trustee said warehouse receipts and any portion of the same; the reasonable value and the wholesale cost price in the City of Los Angeles from and after August 3, 1937, and during the remainder

of the year 1937, of the steel covered by the warehouse receipts enumerated above (delivered by the bankrupt to the claimant) was the sum of $33593.09; the reasonable value of each lot of steel designated in said warehouse receipts, and the wholesale cost price thereof, in the City of Los Angeles from and after August 3, 1937, and during the year 1937, was the amount set out in each of said warehouse receipts opposite each lot increased by 42½/262 of each amount.

The bankrupt paid the claimant the sum of $2930.16 prior to the filing of the petition in bankruptcy, which was applied to the loan of August 5, 1937. Interest on each of the three loans was paid up to and including August 31, 1937. Concurrently with the payment of the above amounts, the claimant caused to be delivered to the bankrupt goods covered by portions of said warehouse receipts to the amount of about $3662.70, based upon cost to the bankrupt. At the time of the filing of the petition in bankruptcy, the bankrupt was indebted to the claimant in the total sum of $14,790.76, of which $74.61 was interest.

Prior to the filing of the petition in bankruptcy, a portion (the exact amount not being shown) of the steel covered by the warehouse receipts was taken into possession by Amerlux Steel Corporation, by virtue of a writ of replevin issued in a claim and delivery action in the Superior Court of the State of California, in and for the County of Los Angeles, entitled Amerlux Steel Corporation, a corporation, plaintiff, vs. Fred Williams, doing

business as General Steel Company, Lawrence Warehouse Company, a corporation, *et al.,* defendants, No. 420-322 in the office of the clerk of said Superior Court.

On February 9th, 1938, appellee filed its Proof of Secured Claim with the Referee, asserting therein that it held the remainder of the steel described in the warehouse receipts as security for an indebtedness of $14,790.76, to which claim the trustee filed objections based upon the Bulk Sales Provisions of section 3440 of the Civil Code, State of California, the pertinent portions of which, as same existed at the time of the instant transactions, are set forth in Appendix A.

A partial hearing was had, at which time the appellee filed its answer in which it asserted that its security consisted of the aforesaid warehouse receipts. The trustee thereupon filed additional objections basing same upon the "no change of possession" provisions of section 3440. After a full hearing, the Referee found the facts which are heretofore set forth, and in addition found that there had been no immediate delivery nor actual and continued change of possession of the steel, and that the warehouse receipts had been received by the appellee for the purpose of avoiding the provisions of section 3440, and that the transactions by the bankrupt and the appellee were otherwise than in the ordinary course of trade and other than in the regular and usual practice and method of business of the bankrupt, and that, therefore, the transfers of the warehouse receipts and the steel described therein were fraudulent and void as against the trustee, and that the

appellee was not entitled to any security for its claim and that the trustee was the owner of, and entitled to, the possession of the warehouse receipts and the steel therein described.

Petition for review was filed by the appellee at a hearing of which the Judge of the District Court confirmed the findings of the Referee, with the exceptions that there had been immediate delivery and actual and continued change of possession of the steel and that the warehouse receipts had not been received by the appellee for the purpose of avoiding the provisions of section 3440, and that the transactions by the bankrupt and the appellee were in the ordinary course of trade and were in the regular and usual practice and method of business of the bankrupt, and that the provisions of section 3440 were not applicable to the instant transactions in that the same were controlled exclusively by the provisions of Uniform Warehouse Receipts Act (Laws 1909, Ch. 290) and that, therefore, the appellee was entitled to its security.

The main questions now presented are: "Was there a violation of either the Bulk Sales or No Change of Possession Provisions of section 3440?", and if so, "Is the Uniform Warehouse Receipts Act exclusive of section 3440?"

Specification of Errors Relied Upon.

The appellant proposes to rely upon Points I, II, III, IV, V and VI of "Statement of Points Upon Which Appellant Intends to Rely" [Tr. of R. pp. 537-538].

ARGUMENT

POINT I.

The District Court Erred in Holding That the Instant Transactions, Based on the Pledging of Substantial Portions of the Stock in Trade of a Wholesale and Retail Merchant, Through the Medium of Pledging Non-Negotiable Warehouse Receipts, Were Not Subject to the Provisions of Section 3440 of the Civil Code of the State of California, and That Said Section Has Been Repealed by the Warehouse Receipts Act of the State of California.

The reversal of the Referee by the District Court proceeded, primarily, upon the assumption that the Warehouse Receipts Act repeals all Acts or parts of Acts inconsistent with it, and that if compliance be had with the terms of the Warehouse Receipts Act it is sufficient to sustain the transactions involved [Tr. of R. pp. 154-155]. Such ruling is premised upon section 60 of the Uniform Warehouse Receipts Act, which reads as follows: ". . . all Acts or parts of Acts inconsistent with this Act are hereby repealed."

The effect of this section is not so broad as it might seem. At the onset reference is made to *Erie Railroad Co. v. Tompkins,* 304 U. S. 64, 114 A. L. R. 1487, in which it is clearly ruled that the Federal Courts are bound on state matters by state decisions.

The subject of repeal of statutes is dealt with in 23 Cal. Jur. commencing at page 686. At page 689 it is stated that "frequently statutes contain a general clause expressly repealing all Acts or parts of Acts in conflict with, or inconsistent with, their provisions, but not re-

pealing by name the provisions of any Act on the same subject matter. Such a repealing clause has no greater force than a repeal by implication."

See:

Matter of Clary, 149 Cal. 732, at 737.

The repeal of statutes by implication is not favored. The rule is "that where there are two laws upon the same subject, they must be so construed as to maintain both, if it can be done, without destroying the evident intent and meaning of the latter Act." See *Traber v. Railroad Commission,* 183 Cal. 310.

Repeals by implication are found to exist only where "it becomes apparent that the legislature did not intend the former Act to remain in force," 23 Cal. Jur. 691.

Washington Lumber Co. v. McGuire, 213 Cal. 13, involved the problem of whether violation of provisions of the California Vehicle Act, sections 45 and 45¼ (Deering's General Laws, 1929 Supp. p. 3441), as the Act then existed, repealed by implication the transfer provision of section 3440, and section 2957 of the Civil Code relating to the form and method of recordation of chattel mortgages.

Section 162 of the Act stated, in part:

> ". . . all Acts, or parts of Acts, in conflict with, or inconsistent with, this Act, are expressly repealed."

Section 45 of the California Vehicle Act read:

> "Until said division shall have issued a new certificate of registration and certificate of ownership as hereinbefore, in division (d) provided, delivery

of such vehicle shall be deemed not to have been made and title thereto shall be deemed not to have been passed, and said intended transfer shall be deemed to be incomplete and not to be valid or effective for any purpose."

It was the contention of the defendant in the above case that section 3440 relating to the transfer of property did not apply to the transfer of a motor vehicle because the California Vehicle Act, passed subsequent to section 3440, provided an exclusive and complete means of transferring such property, because, the defendant contended, section 3440 was repealed by implication upon the enactment of section 45 of the California Vehicle Act.

The court said (page 17):

"the formalities specified in the 'Motor Vehicle Act' cannot be disregarded, and no other formalities will operate to pass the title to a motor vehicle. But it does not follow that the formalities required by the Act were intended to do away with all statutory requirements on sales of personal property, generally. In other words, because these formalities are *essential* to the transfer of title is no ground for concluding that they are *exclusive* of all other restrictive provisions. To say, as the section does, that one requirement cannot be disregarded, is not at all the same as to say that all others may be."

At page 19 it is stated:

"it must be concluded, therefore, that whatever reasons of policy or practical expediency might be advanced in favor of defendant's proposition, the legis-

lature has given no indication of intention to exclude the transfer of motor vehicles from the provisions of section 3440 and, without such an indication, we must hold the section applicable to them."

Subsequent cases to the same effect are:

Bush v. Bank of America, 1 Cal. App. (2d) 588;

Dennis v. Bank of America, 98 Cal. App. Dec. 648 (Sept. 21, 1939).

The only reported case in California, to the knowledge of appellant, on the question of construing section 3440 in a transaction where warehouse receipts have been involved, is *McCaffey Canning Co., Inc., v. Bank of America,* 109 Cal. App. 415, particularly commencing with page 426. Hearing was denied by the Supreme Court on January 8, 1931. A footnote at page 24 of an article entitled "Theory of Field Warehousing," Washington Law Review of January, 1937, refers to the *McCaffey* case (erroneously spelled in footnote as *McGaffey v. Bank of America*) as a "well-considered case reviewing all the authorities." This article was referred to in Prentice Hall Federal Bank Service, 1938, at page 20091 (note 3), as being part of literature, most of which has been written by persons connected with warehousing companies.

The goods of Ventura Canning Company were warehoused with Lawrence Warehouse Company under a form of agreement substantially as in the present case. Upon the issuance of non-negotiable warehouse receipts, same

were pledged with Bank of America National Trust & Savings Association. Question was raised by a creditor as to the failure of Lawrence Warehouse Company and of Bank of America to comply with the "no change of possession" provisions of section 3440.

The court said, in the *McCaffey* case (page 434):

> "Warehousing on the premises of the owner proposing to pledge his merchandise is effective when done in obedience to legal requirements, but when done only far enough to get the goods only represented by documents, rather than to really getting them stored, the documents are but scraps of paper. The term 'field warehousing' is not a talisman to give dominion by enhancement . . . Whether warehousing is called 'field warehousing' or by any other name, it cannot be effectively conducted in this state without compliance with the law as declared in section 3440 of the Civil Code."

It may be true, as stated in *Jewett v. City Transfer & Storage Company,* 128 Cal. App. 556, that the purpose of the Warehouse Receipts Act was to regulate the business of conducting a warehouse; but it does not follow that the Warehouse Receipts Act was intended to regulate, also, the affairs of creditors in a manner, and for purposes, which are not intended in the Warehouse Receipts Act, such as the disposal, by a merchant, of a substantial portion of his stock in trade. Added emphasis is given to the foregoing statement by the conduct of the 1939 session of the Legislature of the State of California.

Assembly Bill 2224, proposing, among other things, to except warehouse receipts transactions from the effect of section 3440, was passed by both houses of the Legislature and sent to the Governor for signature.

Under date of May 19, 1939, Governor Olson replied as follows:

"State of California, Governor's Office
Sacramento, May 19, 1939.

To the Honorable Members of the Assembly, State of California, Sacramento, California:

Greetings:

I am returning herewith, without my signature, Assembly Bill No. 2224, entitled: 'An Act to add section 3440.5 to the Civil Code, relating to pledges and credit transactions'.

My objections to this bill are as follows:

Section 3440 of the Civil Code as it now exists has been a bulwark of protection against commercial frauds. I believe its provisions should not be weakened.

There is no definition of the word 'warehouse' in this bill, and the provisions of section 3440 of the Civil Code could easily be circumvented under this bill by merely storing one's goods in a private warehouse.

If the bill were limited to goods in a public warehouse, provision should be made for the keeping of warehouse records, open to the inspection of all, and particularly of prospective creditors, to show all transactions and the interest of all parties in and to the goods warehoused.

If the bill be construed as exempting all pledge transactions from section 3440 of the Civil Code (and it is open to such construction), such provision is clearly undesirable.

Respectfully submitted,

CULBERT L. OLSON,
Governor of California."

See Assembly Journal, May 19, 1939, page 2263.

Thereafter, by Senate Bill No. 1278, section 3440.5 of the Civil Code was added, being passed by both houses of the Legislature and concurred in by the Governor. That section reads:

"Section 3440 of this code shall not apply to goods in a warehouse where a warehouse receipt has been issued therefor by a warehouseman, as defined in the Warehouse Receipts Act, and a copy of such receipt is kept at the principal place of business of the warehouseman within the city or county in which is located the warehouse in which said goods are stored. Such copy shall be open to inspection upon written order of the owner or lawful holder of such receipt."

Thus it would appear that both the Legislature and the Governor considered that section 3440, as it existed at the time of the instant transactions, was applicable to transactions involving the pledge of warehouse receipts, in spite of the previous enactment of Uniform Warehouse Receipts Act.

POINT II.

The Court Erred in Holding That the Transactions Were in the Ordinary Course of Trade of the Bankrupt, and of Business, and in the Regular and Usual Practice and Method of Business of the Bankrupt.

There does not appear to be any California case which specifically defines that portion of section 3440 referring to "the ordinary course of trade" or "of business" or "the regular and usual practice and method of business of the vendor, transferor or assignor."

Each case involving the bulk sales provisions of section 3440 seems to assume that the particular transactions involved in that case are "other than in the ordinary course of trade, etc."

In *Shelley v. Byers,* 73 Cal. App. 44, the sale of the entire stock was considered to be out of the ordinary course.

In *Schainman v. Dean,* 11 A. B. R. (N. S.) 594, 24 Fed. (2d) 475, decided by the Ninth Circuit in 1928, it was held that a transfer of $4000.00 of goods from a stock of the value of $20,000-$25,000.00 was a substantial portion, within the purview of the statute, and was outside of the ordinary course of trade, particularly in view of several similar transactions at or about the same time.

In *Shasta Lumber Co. v. McCoy,* 85 Cal. App. 472, the particular transaction was held good because the seller was a manufacturer and because it did not appear that

the sale involved was a substantial portion of the stock of the seller, the court saying:

> "The evidence does not show what lumber, if any, Neal & Sons Lumber Company had at the time of the sale."

Thus it would appear that if the seller had been a merchant and if the goods had constituted a substantial portion of its stock, then the finding could have been that the transaction was "out of the ordinary course of trade, etc."

In the *Matter of Lakin,* 12 A. B. R. (N. S.) 677, Referee Kreft of San Francisco said:

> "In a recent case, that of *Abraham Convisser,* case No. 13470 in this court, the bankrupt, a wholesale glass merchant, after selling off at heavy discounts a large part of his stock of trade, transferred, by way of a pledge, what remained for a loan of $10,-000.00. I held that such transfer was in violation of the Bulk Sales Law, the required notice of such transfer not having been given. This case on review was affirmed. Had the bankrupt in such case sold his merchandise to a dealer in his regular manner, I would have reached a different conclusion. I held that it was not in the regular course of this dealer's business to transfer his entire stock in trade for loans. To repeat, using all the merchant's stock in trade with which to pay one debt is not a transfer in the ordinary course of business. The Bulk Sales Law was designed to meet just such transfers which

> operate to deprive creditors of the debtor of any opportunity to take action where a merchant disposes of his business assets out of the usual course, which usual course they had a right to rely upon would be followed when they extended credit."

In the present case it appears that the bankrupt had a stock of goods of the value of approximately $29,000.00; that during the period from April 1, 1937, to September 14, 1937, the bankrupt made 701 sales in amounts ranging from 41¢ to $1779.51, the average amount of each sale being approximately $99.36; that the loan by appellee of August 5, 1937, involved the pledge of receipts covering goods at a cost value of $10,771.34; that a loan by appellee of August 17th, 1937, involved a pledge of receipts covering goods at a cost value of $7342.29; that a loan by appellee of September 2nd, 1937, involved a pledge of receipts covering goods at a cost value of $10,806.12.

It is clear that the business of the bankrupt was that of buying and selling steel goods rather than the pledging of either his goods or warehouse receipts covering such goods.

POINT III.

The District Court Erred in Holding That There Was an Actual, Immediate, and Continued Change of Possession of the Steel Involved Herein.

The referee found that there was no immediate, actual and continued change of possession, as required by the "change of possession" portion of section 3440. The finding of the referee was reversed by the District Court on the theory, apparently [see Memorandum of Order, Tr. of R. 154-156], that the facts herein differed materially from the facts presented in *McCaffey Canning Company v. Bank of America, supra,* and that the warehouse company maintained a real, actual and *bona fide* possession of all the steel, in full compliance with the provisions of the Warehouse Receipts Act of the State of California [Tr. of R. p. 160].

The appellant believes that there is no material difference in facts of the two cases in so far as the change of possession features are concerned.

In the *McCaffey* case the Ventura County Canning Company rented a portion of the building in which its canning operations were carried on. A man named Pace, employed by the canning company, served as its cookroom foreman and superintendent of canning operations at a salary of $60.00 per week. A sub-lease, similar to the one involved here, was made by the canning company with the Lawrence Warehouse Company. The canning company continued to conduct its business as before, Pace being the cookroom foreman and superintendent, and acting as the sole representative of the warehouse company on the premises. At night an employee of the canning company slept on a cot in the office of the canning

company. As cans were filled they were stacked in rows reaching to the ceiling at the south end of the building. There was nothing to separate the canning department from the storage department excepting a space of about 15 feet in width. As the cans were stacked they were inventoried by Pace, who kept the records and issued non-negotiable warehouse receipts for the Lawrence Warehouse Company for the account of Bank of America, appellee herein. Stack cards of the warehouse company were placed on the stacks, showing the quantity, etc., and the statement "warehoused to Bank of America." The receipts were pledged with Bank of America. When fruit was to be marketed, a release was issued by the Los Angeles office of the warehouse company on order of the Bank of America and, upon delivery of the receipt to Pace, the quantity specified was shipped by the canning company to brokers. Pace's salary remained at $60.00 per week and was paid to him by the warehouse company, which, in turn, was reimbursed by the canning company.

There was a sign of the Lawrence Warehouse Company inside the shop and conflicting testimony that there were two signs on the outside of the building.

In the present case Rinne, the general handy man for the bankrupt, continued with his duties, as previously, excepting that he no longer drove a truck, and received the same compensation through the warehouse company, which, in turn, was reimbursed by the bankrupt.

The bankrupt not only kept a large portion of his own goods in the same room as those against which warehouse receipts had been issued, but even, in some instances, intermingled his own goods in the same stacks, piles and bins in which the "warehoused" goods were kept. From

July 20, 1937, at which time the warehouse lease was entered into, until July 28, 1937, at which time a portion of the goods were pledged to California Bank, the bankrupt was permitted full and complete entry to the "leased" premises to the warehouse company, and the unequivocal right to remove and transfer any portion of the goods in the so-called warehouse.

No inventory, or other record, of the goods contained in the warehouse was maintained or kept by the warehouse company. After July 28, 1937, no record or inventory was kept by the warehouse company of any of the goods in the premises other than those against which warehouse receipts had been issued.

Williams, the bankrupt, through Rinne, was permitted to, and he did, keep his free goods in the same stacks, piles and bins as were placed the "warehoused" goods, and was permitted to remove and sell such free goods at his own volition.

The only difference, that we perceive, favorable to the appellee, in the facts of the *McCaffey* case and the present one is that, for the purposes of the nonsuit in the *McCaffey* case, there appeared to be no signs of the warehouse company posted on the inside of the building, and that an employee of the canning company slept in the premises at night. In the present case the facts differ in favor of appellant in that, in many instances, there was no separation of the bankrupt's goods from the "warehoused" goods; and the bankrupt was permitted entry to the premises and the right to remove and sell free goods, at his pleasure.

There are numerous authorities outside of California, pro and con, as to the effect of employment by a ware-

house company as custodian of a former employee of the pledgor. In this instance it will be noted that Rinne was not only a *former* employee, but, to all intent and purpose, was actually an employee of the bankrupt during the time of the transactions herein involved.

The *McCaffey* case, at page 436, says:

> "The appointment of the owner, or one of his staff, as a warehouse custodian of goods stored, while not conclusively ineffectual, is, nevertheless, an instance to give pause, and must be weighed carefully in connection with the other facts in evidence. (*Goldstein v. Nunan,* 66 Cal. 524, 544; *Hickey v. Coschina,* 133 Cal. 81, 84; *Bucher v. Allen,* 11 Cal. App. 650, 651; *Vail v. Nichibei Bussan Co.,* 65 Cal. App. 60, 63; *Gray v. Little*, 97 Cal. App. 442, 449."

It is true that numerous signs, indicating that the Lawrence Warehouse Company was in possession of all the goods on the premises, were posted on the interior of the warehouse and on the outer premises surrounding the building. Doubtless, such signs would tend to place third persons on notice, but, it seems to the appellant, that the ensuing course of the bankrupt, whereby, without any apparent restraint, he intermingled his goods in the various stacks, piles and bins on which were placed stack cards, and proceeded to sell or transfer such goods freely, would vitiate any notice to a third person which such signs might have given. To allow the bankrupt to keep his own goods, to which he had access, or over which he exercised any rights of possession, in the same premises with "warehoused" goods is inconsistent with the concept of exclusive control by the warehouse company.

> *Prentice-Hall Federal Bank Service,* para. 20091, p. 20099.

It is respectfully urged that the referee, as the trier of the facts, was, in effect, the jury referred to in the *McCaffey* case and, there being sufficient evidence upon which to make a finding of no immediate, actual and continued change of possession, his finding to that effect was conclusive and, therefore, the District Court erred in reversing such finding and substituting therefor the findings complained of.

POINT IV.

The District Court Erred in Failing to Follow the Decisions of the Highest Appellate Courts of the State of California Involving Construction of Section 3440.

The argument on this point is based upon the decision of *Erie Railroad Company v. Tompkins,* 304 U. S. 64, 114 A. L. R. 1487, and involves the ruling of the District Court that the instant transactions are not subject to the provisions of section 3440, and that the Uniform Warehouse Receipts Act is exclusive of section 3440.

Washington Lumber Co. v. McGuire, supra, 213 Cal. 13, at 17;

McCaffey Canning Co. v. Bank of America, supra.

POINT V.

The District Court Erred in Holding That the Transactions Were Not Fraudulent and, Therefore, Not Void as Against the Appellant and Creditors Generally.

This point is based upon the errors of the District Court referred to in Points I, II, III and IV, and no further discussion will be had.

POINT VI.

The District Court Erred in Holding That Appellee Is a Secured Creditor.

This point is based upon the errors of the District Court referred to in Points I, II, III, IV and V.

Conclusion.

In conclusion, therefore, the appellant submits that the order and findings of the referee were correct, and that the order and findings of the district judge, in so far as same reversed the order and findings of the referee, are erroneous in that:

(a) The Uniform Warehouse Receipts Act is not exclusive of section 3440.

(b) The pledging, to the appellee, by means of warehouse receipts, of a substantial portion of the stock in trade of the bankrupt, without the notice required under section 3440, was out of the usual course of trade and in violation of the bulk sales provisions of said section 3440.

(c) The possession maintained by the warehouse company, and appellee, was not the possession required under the provisions of section 3440.

Appellant respectfully submits that the findings and order of the referee are correct, and that the findings and order of the District Court reversing the findings and order of the referee are erroneous, and that the latter should be reversed, and the findings and order of the referee confirmed.

Respectfully submitted,

RUSSELL B. SEYMOUR,

Attorney for Appellant.

APPENDIX A.

"Every transfer of personal property, other than a thing in action, or a ship or cargo at sea or in a foreign port, and every lien thereon, other than a mortgage, when allowed by law, and a contract of bottomry or respondentia, is conclusively presumed if made by a person having at the time the possession or control of the property, and not accompanied by an immediate delivery, and followed by an actual and continued change of possession of the things transferred, to be fraudulent, and therefore void, against those who are his creditors while he remains in possession, and the successors in interest of such creditors, and against any person on whom his estate devolves in trust for the benefit of others than himself, and against purchasers or encumbrancers in good faith subsequent to the transfer; . . ."

"Provided, also, that the sale, transfer, or assignment of a stock in trade, in bulk, or a substantial part thereof otherwise than in the ordinary course of trade and in the regular and usual practice and method of business of the vendor, transferor, or assignor, and the sale, transfer, assignment or mortgage of the fixtures or store equipment of a baker, cafe or restaurant owner, garage owner, machinist, or retail or wholesale merchant, will be conclusively presumed to be fraudulent and void as against the existing creditors of the vendor, transferor, assignor or mortgagor, unless at least seven days before the consummation of such sale, transfer, assignment or mortgage, the vendor, transferor, assignor or mortgagor or the

intended vendee, transferee, assignee or mortgagee, shall record in the office of the county recorder in the county or counties in which the said stock in trade, fixtures or equipment are situated a notice of said intended sale, transfer, assignment or mortgage, stating the name and address of the intended vendor, transferor, assignor or mortgagor, and the name and address of the intended vendee, transferee, assignee or mortgagee, and a general statement of the character of the merchandise or property intended to be sold, assigned, transferred or mortgaged, and the date when and the place where the purchase price or consideration, if any there be, is to be paid."